A

MAJLIS AMANAH RAKYAT

v.

BASS BIN LAI

B

HIGH COURT SABAH & SARAWAK, SIBU
HAMID SULTAN ABU BACKER JC
[ORIGINATING SUMMONS NO: 24-64-2007]
10 FEBRUARY 2009
[2009] CLJ JT(1)

C

BANKING: *Islamic banking - Bay al Inah facility - Foreclosure of charged property - Whether facility contravened riba rule - Challenge to application - Whether to be taken vide originating process - Order for sale - Whether to be allowed - Land Code (Cap 81) (Sarawak), s. 148 -* D *Contracts Act 1950, s. 66*

By the Bay al Inah facility secured upon a third party charge herein ('the facility'), the plaintiff agreed to sell some assets to the customer for RM24,137.81 upon deferred payment and then repurchased same for cash payment of RM21,000. The customer E defaulted in the repayment and following that the plaintiff applied to foreclose the property under s. 148 of the Sarawak Land Code ('SLC'). Before the learned Judicial Commissioner, the defendant chargor objected to the application arguing, presumably, that the facility, having transgressed the riba rule, was prohibited in Islam. F The plaintiff retorted that notwithstanding that the proceeding was predicated upon the provisions of the SLC and pertained to Islamic banking facilities, the court should apply the same principles as applicable in conventional banking facilities. Alternatively, it was argued that even upon the assumption that the facility was tainted G with riba or contravened Islamic commercial or banking principles, the court could still follow *Arab-Malaysia Finance Bhd v. Taman Ihsan Jaya Sdn Bhd* ('*Taman Ihsan*'s case), invoke s. 66 of the Contracts Act 1950 and grant an order for sale for the sum of RM21,000. H

Held (allowing order for sale as prayed):

(1) The general complaint in respect of transactions such as Bay al Inah is that the sale is fictitious and that the whole purpose I is to grant a loan with profits thereby breaching the riba rule. The riba rule does not permit one to earn a profit directly from cash transactions unless it is a trade-related transaction with the employment of capital, labour and risk. (para 6)

(2) The proper procedure to challenge the legality of a contract is by filing an originating process and seeking relief as set out in the Specific Relief Act 1950. However, that does not mean that the court has no power or jurisdiction to consider such issues if properly raised or argued in a foreclosure proceeding (see *Taman Ihsan*'s case). Only that in such proceeding, the court is focused on whether to allow the application for foreclosure as prayed or restrict the sum claimed according to the justice of the case and will not *per se* make any declaratory order if there is no counterclaim for declaratory relief to set aside, annul or declare the contract null and void. (para 8)

(3) The challenge to the contract here was not taken according to law for curial scrutiny as to whether the contractual terms said to be pursuant to Bay al Inah was in fact shariah compliant, and there was thus no necessity for the court to deal with the issue. However, for the purpose of the relief, and bearing in mind *Malayan Banking Bhd v. Ya'kup Oje & Anor*, the court could still consider whether the sum claimed is equitable. (para 8)

(4) The plaintiffs averred that the tenure of the facility had expired and in consequence there is no issue of rebate arising with the result that the sum prayed should be allowed. There was merit in this submission and the court would hence allow the plaintiff's originating summons as prayed. (para 9)

Obiter:

(1) The law of contract does not recognise fictions or legal tricks and there is a greater prohibition in the Holy Qur'an and Hadiths to ensure that legal tricks and fictions are not used to defeat justice, equity or the Qur'anic commands. (para 8)

(2) The common notion that the Islamic jurists or the Shariah Advisory Boards were the sole arbiter for determining whether a shariah financial instrument is shariah compliant is flawed. The court is the supreme body to decide what is right and what is wrong in a given circumstance, and hence, is the final decision maker to decide whether a contract or an Islamic product based on Murabaha, Bay al Inah or Mudarabah principles as the case may be is valid or otherwise. (para 8)

A **(3)** Most often nowadays, bankers and traders, with the help of contemporary Islamic jurists or lawyers, for fiscal reasons, are keen to give prime recognition to obscure, unacceptable and/or dubious concepts which are not recognised by the Holy Qur'an or Sunnah or by the vast majority of the Muslim
B jurists. This is done primarily to make profits using the shariah label. It must be asserted that in the history of Islamic jurisprudence, honest solutions to contemporary problems would generally be accepted by the Muslim majority, whilst dubious concepts or arguments to justify a wrong are often
C seen as heretical by the majority. (paras 8 & 9)

Case(s) referred to:

Arab-Malaysian Finance Bhd v. Taman Ihsan Jaya Sdn Bhd & Ors; Koperasi Seri Kota Bukit Cheraka Bhd (Third Party) And Other Cases [2009] 1 CLJ 419 HC ***(refd)***

D *Bank Kerjasama Rakyat Malaysia Bhd v. Emcee Corporation Sdn Bhd* [2003] 1 CLJ 625 CA ***(refd)***

Malayan Banking Bhd v. Ya'kup Oje & Anor [2007] 5 CLJ 311 HC ***(refd)***

Shamil Bank Bahrain v. Beximo Pharmeticals Limited & Ors [2003] EWHC 2118 ***(refd)***

E *Yong Fuat Meng v. Chin Yoon Kew* [2008] 5 CLJ 705 HC ***(refd)***

Legislation referred to:

Contracts Act 1950, s. 66

Land Code (Cap 81) (Sarawak), s. 148

F **Other source(s) referred to:**

Critical Thoughts: Legislative Intervention Imperative To Support Islamic Financing On A Global Scale, [2009] 1 MLJ 1xiii

Professor Dr Engku Rabiah, *Bay Al-Inah and Tawarruq, Essential Reading In Islamic Finance,* [2008], CERT Publication, p 136

G *The application of Bay Al-Inah and Bay Al-Dayn in Malaysian Islamic Bonds. An Islamic Analysis,* International Journal of Islamic Financial Services Vol 2

For the plaintiff - Lim Choun Hong; M/s Chan, Jugah, Hoo & Co Advocates
For the defendant - In person

H *Reported by Wan Sharif Wan Ahmad*

I

JUDGMENT

Hamid Sultan Abu Backer JC:

[1] This is my judgment in respect of the plaintiffs' originating summons to foreclose the property under s. 148 of Sarawak Land Code (SLC) which was given as a third party charge in relation to a banking facility under the Islamic principles of Bay al Inah. I have dealt with this area of law in great detail, in two judgments namely (i) *Malayan Banking Bhd v. Ya'kup Oje & Anor* [2007] 5 CLJ 311 (ii) *Yong Fuat Meng v. Chin Yoon Kew* [2008] 5 CLJ 705 (See article, *Critical Thoughts: Legislative Intervention Imperative To Support Islamic Financing On A Global Scale* [2009] 1 MLJ 1xiii) I do not wish to repeat the concepts, principles, jurisprudence and rationale etc. stated in these cases in relation to Islamic Banking save to say that this judgment must be read with those two judgments for purpose of comprehensiveness only.

[2] On the day of hearing, the defendant's representative was present in court and objected to the application, without filing any affidavit or submission.

[3] Brief Facts

(a) The plaintiffs at the request of the customer had agreed to grant the sum of RM21,000 in accordance with the Islamic principles of Bay al Inah ("the said facility") to the said customer whereby the plaintiffs shall sell an asset to the said customer on a deferred payment and then the plaintiffs shall immediately re-purchase the assets for cash at a discount. Pursuant to the said facility, the plaintiffs had entered into two agreements namely, a Property Sale Agreement and a Property Purchase Agreement. Pursuant to the said Property Sale Agreement, the plaintiffs agreed to sell one unit of Proton Saga and Suzuki Jeep ("the said property") and the said customer agreed to purchase the said property at a sale price of RM24,137.81 by deferred payment that was to be paid by way of 48 monthly instalments of RM502.87 each ("the sale price"). However, no payment was made to the plaintiffs and the tenure of the 48 months had also expired and lapsed. By the said Property Purchase Agreement, the plaintiffs had agreed to re-purchase the said property for cash at a discount in the sum of RM21,000 in accordance with the Islamic principles of Bay al Inah. The aforesaid transaction was

A further secured by way of a charge executed by a third party chargor, the defendant in this action. As the said customer and the chargor had defaulted in the repayment of the sale price under the said facility, the plaintiffs had filed this action. The defendant who has died after the commencement of this
B proceeding, was represented by a personal representative by order of court. When the case came for hearing, the parties were ordered to file written submission to justify whether the facility is shariah compliant, to provide the appropriate relief in view of the recent High Court case of *Arab-Malaysian Finance*
C *Bhd v. Taman Ihsan Jaya Sdn Bhd & Ors (Koperasi Seri Kota Bukit Cheraka Bhd, third party)* [2008] 5 MLJ 631 *(Taman Ihsan)* where it was held:

(i) When dealing with cases involving Islamic financing facilities,
D the civil court functions strictly as a civil court and does not become a Syariah Court. The civil court's function, in this regard, is to render a judicially considered decision before it according to law and not apply Islamic law as if it were a Syariah Court. Its function is to examine the application of the Islamic concepts and to ensure that the transactions in
E the cases before it do not involve any element not approved in Islam

(ii) In Islamic financing there is nothing that prohibits the giving of a loan. It is only the riba element in the loan that is
F prohibited. Hence, loans without riba ie benevolent loans or qard al-Hasan are allowed

(iii) The term Al-Bai' Bithaman Ajil is no more than a sale and deferred payment of the price as agreed to between the parties. As such, the selling price is ordinarily paid upon
G delivery. However if the payment is to be made later, the seller is in effect extending a credit or a loan of that selling price. At the same time it must be remembered that the deferred payment of the selling price is a credit or a loan permissible only because no riba is charged. Furthermore, the key to the argument that the Al-Bai' Bithaman Ajil scheme
H does not involve any element not approved by Islam is to read the PSA independently. Therefore it is essential to maintain a *bona fide* sale in order that the profit or selling price should not be an element disapproved by Islam. Even so, an interpretation of the selling price must not be such as to impose a heavier burden than on a loan with interest
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(iv) The court has the authority to look beyond the words of the agreement to the actual facts of the case in order to determine the substance of the transaction between the plaintiffs and the defendants before it draw any conclusions on the nature of the Al-Bai' Bithaman Ajil transactions. It is necessary to look beyond the labels used and look at the substance particularly in the light of the fact that the interpretation advanced by the plaintiffs resulted in the defendants being burdened with a debt far in excess of that if they had taken interest based on a conventional loan).

(v) Thus when the bank became the owner of the property by a direct purchase from the vendor or by a novation from its customer, as in the present cases, and then sold the property to the customer, the plaintiffs' interpretation of the selling price ought to be rejected and the equitable interpretation applied. Where the bank purchased directly from its customer and sold back to the customer with deferred payment at a higher price in total, the sale was not a *bona fide* sale but a financing transaction and the profit portion of such an Al-Bai Bithaman Ajil transaction rendered the facility contrary to the Islamic Banking Act 1983 or the Banking and Financial Institutions Act 1989, as the case may be.

(vi) Since the plaintiffs' actions resulted most likely from a misapprehension rather than intent afterthought, the plaintiffs were entitled under s. 66 of the Contracts Act 1950 to a return of the original facility amount they had extended. It was equitable that the plaintiffs seek to obtain a price as close to, if not more than, the market price as possible, and account for the proceeds to the respective defendants

Plaintiffs' Argument

[4] The learned counsel for the plaintiffs says that the foreclosure proceeding is made pursuant to SLC. Although it is related to Islamic Banking facilities, the plaintiffs assert that the court must apply the same principle as done for conventional banking facilities and relies on the case of *Bank Kerjasama Rakyat Malaysia Bhd v. Emcee Corporation Sdn. Bhd* [2003] 1 CLJ 625 where the Court of Appeal observed:

> As was mentioned at the beginning of this judgment the facility is an Islamic banking facility. But that does not mean that the law applicable in this application is different from the law that is applicable if the facility were given under conventional banking. The charge is a charge under the National Land Code. The

A remedy available and sought is a remedy provided by the National Land Code. The procedure is provided by the Code and the Rules of the High Court 1980. The court adjudicating it is the High Court. So, it is the same law that is applicable the same order that would be, if made, and the same principles that should be applied in deciding the application.

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[5] Further, the learned counsel says that the decision made in *Taman Ihsan*'s case or other cases which dealt with rebates will not apply in the instant case, as the tenure of the facility has been completed. In the alternative, the learned counsel says that if the C court takes the view that the bay al inah principles contravene Islamic principles then to grant an order for sale for the sum of RM21,000 based on s. 66 of Contract Act 1950 (CA 1950), as was done by the learned judge in *Taman Ihsan*'s case.

D **Bay Al Inah**

[6] The term 'bay' means sale. Bay al inah transaction generally means a sale followed by a buy back transaction at a discounted price. The contemporary practices by Islamic financial institutions E can be said to be an agreement where the financer purportedly sells an asset to the customer on a deferred payment and then the financer immediately repurchases the asset for cash at a discounted price. The general complaint in respect of such transaction is that, the sale is fictitious and the whole purpose is F to grant a loan with a profit. In consequence, it breaches the 'riba' rule. In essence, the 'riba' rule does not permit one to earn profit directly from cash transactions, unless it is a trade related transaction with the employment of capital, labour and risk.

[7] Much literature on the subject, inclusive of the concept of G bay al inah is found in books, articles and web sites. (see articles by Dr. Rani Kamarudin [2007] 6 MLJ IXXVI; Dr. Ashgar Ali [2008] 6 MLJ xiv). The learned jurist, author and well known Islamic scholar in Malaysia Dr. Saiful Azhar Rosly and Mohmood M. Sanusi has captured the argument in a nut shell in the article H *"The application of Bay Al-Inah and Bay Al-Dayn in Malaysian Islamic Bonds. An Islamic Analysis"* (International Journal of Islamic Financial Services" Vol. 2) as follows:

Bay al-inah is generally known as sale based on the transaction I of Nasi'ah (delay). The (prospective) debtor sells to the (prospective) creditor some object for cash which is payable immediately; the debtor immediately buys simultaneously the same

> object for a greater amount for a future date. (13) Thus the transaction amounts to a loan. The difference between the two prices represent the interest. Such contract was evolved in the early period of Islam and it exists for the fundamental reason that a loan for interest is forbidden because it is equivalent to usury (riba). (14) In this contract, there is an economic interest for both the borrower and the lender, which at the same time circumvents the prohibition of usury.
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> The issue which concerns us here, is how does Islamic law view such contract: whether the sales be allowed *prima facie*, or disallowed because the motive behind the sales is to legalize that which is illegal or usurious.

Associate Professor, Dr. Engku Rabiah in her article "*Bay Al-Inah and Tawarruq* (see *Essential Reading In Islamic Finance*", [2008], CERT Publication) at p. 136 says:

> In terms of the Islamic legal rules on bay'al-'inah, it has been welknown that the Shafi'i school of Islamic law legalized and validated bay' al-'inah transactions, though some of them considered the practice as discouraged (makruh). Following the same, the Shari'ah Advisory Council (SAC) of the Malaysian Securities Commission (SC) and the National Shari'ah Advisory Council (NSAC) of the Central Bank of Malaysia (Bank Negara Malaysia – BNM) had officially endorsed bay'al-inah transactions in their legal rulings and resolutions. One of the arguments raised to support their adoption of the Shafi'is view in legalizing bay' al' inah is public interest consideration (maslahah), ie, to overcome the problem of liquidity shortage in the country, without having to resort to conventional riba-based borrowing. The legalization of bay'al'inah may also be said to be in line with the legal maxim on the lesser of two evils (akhaf al dararain)
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> Nevertheless, it is also well known that the legality and validity of bay'al'inah is not an agreed matter amongst the jurists of Islam. The controversy on bay'al'inah had been elaborately documented in many Islamic fiqh manuals.

[8] I have read the originating summons, affidavit and submission in detail. On the facts of this case, I think it will be a proper exercise of judicial discretion to allow the application without any curial scrutiny of the facility document in this action. My reasons are as follows:

A (a) The law of contract does not recognise fictions or legal tricks. There is a greater prohibition in the Holy Qu'ran and Hadiths to ensure that legal tricks and fictions are not used to defeat justice, equity and/or Qur'anic commands. The only persons within the Islamic academia who propounded legal tricks or
B fictions are a small number of isolated jurists, who by themselves were able to justify their conclusion based on the trade practice of that particular area, taking into consideration the need and necessity and justifying their action with some related jurisprudence. Most often nowadays, Bankers cum
C traders, with the help of some contemporary Islamic jurists/or lawyers, for fiscal reasons, are keen to give prime recognition to obscure, unacceptable and/or dubious concepts which are not recognised by the Holy Qu'ran and/or Sunnah or by the vast majority of the muslim jurists. This is done primarily to
D make profits using the shariah label. What is surprising is that the jurists or the shariah advisors themselves who have approved this product, attempt to justify this product. The learned justice and scholar Mohamed Taqi Usmani, has captured this concern in the following words:

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> Undoubtedly, Shariah supervisory boards, academic councils, and legal seminars have given permission to Islamic banks to carry out certain operations that more closely resemble stratagems than actual transactions. Such
F permission, however, was granted in order to facilitate, under difficult circumstances, the figurative turning of the wheels for those institutions when they were few in number [and short of capital and human resources]. It was expected that Islamic banks would progress in time to genuine operations based on the objectives of an Islamic
G economic system and that they would distance themselves, even step by step, from what resembled interest- based enterprises. What is happening at the present time, however, is the opposite. Islamic financial institutions have now begun competing to present themselves with all of the same characteristics of the conventional, interest-based
H marketplace, and to offer new products that march backwards towards interest-based enterprises rather than away from these. Oftentimes these products are rushed to market using ploys that sound minds reject and bring laughter to enemies.

I

Is it a correct proposition for muslims, more importantly jurists to support a product which is not shariah compliant and tainted with riba? The answer to some extent is adumbrated in *Taman Ihsan*'s case. It must be asserted that Islam being a universal religion, imposes an obligation on muslims to live within the precinct of Islamic Constitution as set out in the Holy Qur'an. No form of compromise can be recommended to a muslim. Unlike other major religions, Islamic jurisprudence has developed an advanced legal code based on religious injunctions contained in the Holy Qur'an and the Sunnah. Al-Qur'an, (ash-shura: 13) states:

> He had ordained (syariah) for you that religion which the commanded unto Noah, and that We inspire in thee (Mohamed), and that which We commanded unto Abraham and Moses and Jesus.

Al-Qur'an, (al-Jathiya: 18) reads:

> And now have we set thee [0 Mohamedj on a clear road of (our) commandment (shariatin-min-al-amr); so follow it and follow not the whims of those who know not

From the above verses, it is not difficult to appreciate the sentiments of the muslim community for wanting to comply with Islamic principles and law.

(b) There is a common notion in Malaysia that it is in the hands of Islamic jurists and or shariah advisory boards to be the sole arbiter to determine whether a shariah financial instrument is shariah compliant. Such a notion is flawed, and support for the proposition can be found in Justice Khan's report in *Shamil Bank Bahrain v. Beximo Pharmaceuticals Limited & Ors* [2003] EWHC 2118 case where it was stated in no uncertain terms, that in shariah there is no opinion of any person, body or jurist which binds a court in deciding a shariah issue. Further the court is the supreme body under the Federal Constitution to decide what is right and what is wrong in a given circumstances. The Federal Constitution does not permit the courts to abdicate its role by submitting to decisions of lesser bodies or tribunals such as the instant case to shariah supervisory board or fatwas or any purported legislation, rules etc. made thereunder. Having said that, courts will at all times listen receptively to the views and opinions expressed by these bodies but the final decision maker under the Federal

A Constitution is none other than the courts. In essence, whether a contract or Islamic product, based on murabaha or bay al inah or mudarabah etc., principle is valid must be decided by the courts. As long as it does not breach the Qur'anic prohibition of riba or gharar etc., the courts will have
B no hesitation in upholding the same. It all depends on the terms of the contract and not the concept *per se*, because, the court is concerned with the terms and not the concept.

(c) The proper procedure in law to challenge the legality of a
C contract, is by filing an originating process and seeking relief as set out in the Specific Relief Act 1950. That does not mean that the court has no power or jurisdiction to consider such issues if properly raised and argued in a foreclosure proceeding, as was done in *Taman Ihsan*'s case. However in a
D foreclosure proceeding, the court is focused on whether to allow the application for foreclosure as prayed or restrict the sum claimed at its discretion according to the justice of the case. (See *Ya'kup*'s case). The court *per se* will not make declaratory order when there is no counterclaim for
E declaratory relief to set aside, annul or declare the contract null and void etc., in the legal sense save for the purpose of providing the appropriate relief and remedy in a given circumstance, as was done in an articulate manner by the learned judge in the case of *Taman Ihsan*. The relief was
F provided pursuant to s. 66 of Contracts Act which reads as follows:

> **Obligation of person who has received advantage under void agreement, or contract that becomes void**
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> G When an agreement is discovered to be void, or when a contract becomes void, any person who has received any advantage under the agreement or contract is bound to restore it, or to make compensation for it, to the person from whom he received it.

H (d) In the instant case, the challenge to the contract was not taken according to law for curial scrutiny as to whether the contractual terms said to be pursuant to bay al inah was in fact shariah compliant. Thus it is not necessary for me to deal with the issue. However, for the purpose of the relief I can
I consider whether the sum claimed is equitable as done in

Ya'kup's case. In this respect the learned counsel for the plaintiffs say that the tenure of the facility had expired and in consequence there is no issue of rebate and the sum as prayed must be allowed. The plaintiffs' submission has merits.

[9] For reasons stated above, I allow the plaintiffs' originating summons as prayed. *En passant* I will say Parliament is at liberty to enact laws for economic reason or for liquidity purpose or need and necessity as often advocated by jurists/and or lawyers in support of concepts which are often criticised to be tainted with riba. For example, the law can permit cash sale and immediate buy back agreement with discount without saying it is shariah compliant. However, when shariah label is used for a product which is said to be tainted with riba and is said to be shariah compliant, then it will be objectionable, and the court is obliged to act accordingly under the Federal Constitution. As there are too many Islamic financial products in the market which are said to be an infringement of the Qur'anic injunction and/or Sunnah of the Holy Prophet, and there is rampant challenge in court, it is timely for parliament to pass law to address this issue. And provide adequate relief if such products are found by the courts to have infringed the riba rule. The relief to financers may be such as compensation according to market rate etc, wider than that envisaged in s. 66 of the Contracts Act 1950, provided it is just and equitable. It must be asserted here that in the history of Islamic Jurisprudence, honest solutions to a contemporary problem is generally accepted by Muslim community. However, dubious concepts or arguments to justify a wrong are often seen as heretical by the majority.